

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

MODIFICATION TO WESTERN KENTUCKY)	
GAS COMPANY, A DIVISION OF ATMOS)	
ENERGY CORPORATION (WKG) GAS COST)	CASE NO. 97-513
ADJUSTMENT TO INCORPORATE AN)	
EXPERIMENTAL PERFORMANCE-BASED)	
RATEMAKING MECHANISM (PBR))	

ORDER

On December 19, 1997, Western Kentucky Gas Company ("Western") filed its application with the Commission to include an experimental performance-based rate-making ("PBR") mechanism in its tariffs. During a three-year experimental period, the proposed PBR would provide an incentive for Western to lower its gas cost to the fullest extent possible. Western's gas procurement performance would be measured against market-based benchmarks, with Western and its customers sharing equally in any savings achieved or expenses incurred as measured against the established benchmark. The PBR mechanism proposed by Western had an effective date of January 19, 1998. The Commission suspended the tariff for five months and held a hearing on May 6, 1998. The Office of the Attorney General ("AG") and Kentucky Industrial Utility Customers ("KIUC") were granted intervention in the proceeding.

Western's goals for its PBR plan are lower regulatory costs, up-front regulatory oversight as opposed to after-the-fact prudence reviews, successful cost management, an environment in concert with the transition to a more competitive local service structure, and

improving service quality which benefits each customer group. It also cited objectives of sending clear signals through establishment of benchmark standards, using market-based benchmarks to assure prudent performance, and using external criteria to provide a better measurement of performance.

Western's proposed PBR plan includes most components of its gas cost. The mechanism is composed of three distinct mechanisms and a balancing adjustment. Part A is an incentive mechanism for gas commodity costs. Part B is an incentive mechanism for pipeline transportation costs, which includes capacity release. Part C is an incentive mechanism for off-system sales. Part D is the balancing adjustment which will true up the over- and under-collection of amounts billed through Parts A through C.

After considering the evidence of record in this case and being advised, the Commission finds that:

1. Western's PBR Part A – Gas Commodity Costs should be approved as proposed, with the understanding that no labor-related expenses or those typically classified as O&M expenses will be recovered through the Gas Cost Adjustment ("GCA") mechanism.

2. Western's PBR Part B – Transportation Costs should be approved as proposed with the understanding that the benchmark for pipeline transportation costs should be calculated using any discounted rate that it is currently being charged by any pipeline supplier, so that it does not immediately profit from simply maintaining the status quo. Western indicated at the hearing that its intention was to so calculate this benchmark.

As previously stated, no labor-related or O&M expenses are to be recovered through the GCA.

3. Western's PBR Part C – Off-system Sales should be approved as proposed, with no labor-related or O&M expenses to be included for recovery through the GCA. Additionally, the tariff correction proposed by Western at the hearing of this case should be approved so that the Out-of-Pocket Storage Costs associated with Tennessee Gas Pipeline No-Notice Service will be priced at the average price of the gas in storage.

4. Western's Part D – Balance Adjustment should be approved as proposed.

5. Due to the experimental nature of this program, reporting requirements should be imposed. To properly monitor this mechanism, Western should file a quarterly report containing details of each transaction entered into along with spreadsheets and all supporting schedules intended to be used for tracking transactions for each component of the PBR. Affiliate transactions should be separately identified. Western should include with its reports a narrative explanation of transactions, including any use of financial instruments and hedging activities, and with special attention given to transportation opportunities chosen and rejected.

6. In a letter dated May 18, 1998 addressed to the Commission's General Counsel, Western stated that its parent, Atmos Energy Corporation, operates under a "Code of Affiliate Conduct" in the state of Georgia. It also indicated that it voluntarily follows this same code, for the most part, in transactions in other states. In order to ensure that affiliate transactions are conducted "at arm's length" pending the Commission's adoption of an appropriate code of conduct for all utilities, Western should comply with

every section of the Code for Affiliate Conduct which is required by the Georgia Public Service Commission.

7. During the hearing and in correspondence concerning this case, the AG requested that Western provide its customers with a circular explaining the PBR mechanism and the effect the mechanism will have on their rates. The AG also requested that a 1-800 telephone number be listed on the bill so that customers can call with questions about the mechanism. During the hearing and in correspondence, Western indicated that it had no conceptual problems with these requests. Western should file into the record of this proceeding the circular it prepares for its customers and verify that a 1-800 number has been published, on bills or in the circular, for customers who have questions about the program.

IT IS THEREFORE ORDERED that:

1. Western's proposed Experimental Performance-Based Ratemaking Mechanism as approved herein is approved for a period of three years effective on and after the date of this Order.

2. Within 30 days of the date of this Order, Western shall file its revised tariffs reflecting the Experimental Performance-Based Ratemaking Mechanism as approved herein.

3. Western shall file reports as directed herein.


4. Within 60 days of the date of this Order, Western shall file with this Commission the circular it prepares to inform its customers of the PBR.

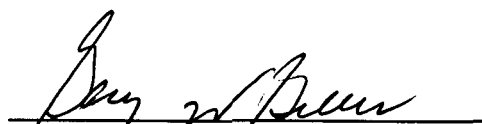
5. At the end of the experimental period Western shall file with this Commission the cumulative results of the PBR program along with its assessment of its success in realizing its stated goals and objectives.

Done at Frankfort, Kentucky, this 1st day of June, 1998.

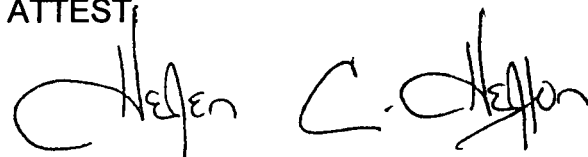
PUBLIC SERVICE COMMISSION


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Vice Chairman


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ATTEST:



Executive Director